

## Message Text

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ACTION ARA-20

INFO OCT-01 ISO-00 AID-20 EB-11 NSC-10 RSC-01 CIEP-02

TRSE-00 SS-15 STR-08 OMB-01 CEA-02 CIAE-00 COME-00

FRB-02 INR-10 NSAE-00 XMB-07 OPIC-12 LAB-06 SIL-01

L-03 H-03 PA-03 PRS-01 USIA-15 RSR-01 /155 W

----- 131052

R 041120Z SEP 73

FM AMEMBASSY BRASILIA

TO SECSTATE WASHDC 9474

INFO AMCONSUL RIO DE JANEIRO

AMCONSUL SAO PAULO

LIMITED OFFICIAL USE BRASILIA 5695

E.O. 11652: N/A

TAGS: EFIN, BR

SUBJECT: REACTIONS TO NEW CAPITAL MARKET INCENTIVES

REF: BRASILIA 5537

1. CONGEN RIO HAS PROVIDED FOLLOWING REPORT BASED ON DISCUSSIONS WITH LOCAL BANKING AND ACCOUNTING FIRMS.

2. GENERAL VIEW IS THAT AUGUST 20 DECREE, ESPECIALLY WHEN COMBINED WITH OTHER MEASURES BEING PREPARED, WILL SIGNIFICANTLY STIMULATE CAPITAL MARKET. PUBLIC LIKELY SHIFT FUNDS FROM FINANCE COMPANIES AND BANK TIME DEPOSITS INTO CAPITAL MARKET, PARTICULARLY GIVEN INCREASE ANNOUNCED AUGUST 23 IN INCOME TAX ON REVENUE FROM SHORT TERM FIXED INCOME PAPER. SEVERAL COMPANIES, MORE CONFIDENT OF PUBLIC ACCEPTANCE, REPORTEDLY PREPARING NEW STOCK ISSUES. GOVERNMENT ALSO LIKELY TO INCREASE ITS EMPHASIS ON MARKET PARTICIPATION BY MUTUAL FUNDS AND INSTITUTIONAL INVESTORS. (COMMENT: INCOME TAX HIKE FROM 10 TO 14 PERCENT ON HIGHLY POPULAR 180 TO 269 DAY BILLS OF EXCHANGE (LETRAS DE CAMBIO), IN ADDITION TO

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REDUCING TAX ADVANTAGE OVER STOCK MARKET INVESTMENTS,

MAY ALSO DAMPEN HIGH CURRENT DEMAND FOR CONSUMER DURABLES BY LIMITING CREDIT AVAILABILITY.)

3. IMMEDIATE IMPACT ON STOCK MARKET TAPERED OFF TOWARD END OF WEEK DUE MAINLY TO PROFIT TAKING. ONE COMMENTATOR EXPRESSED SOME PREOCCUPATION THAT NEW MEASURE MANY OVER-STIMULATE MARKET, BUT THIS TENDENCY LIKELY TO BE ATTENUATED BY GRADUAL IMPLEMENTATION NEW MEASURE. IN FACT, DEBENTURES MARKET NOT EXPECTED TO GROW SIGNIFICANTLY FOR APPROXIMATELY NINE MONTHS. A BRAZILIAN BANKER TERMED INITIAL IMPACT OF INCENTIVE PROGRAM AS PSYCHOLOGICAL AND SAID REAL EFFECTS WOULD BE KNOWN EARLY NEXT YEAR WHEN COMPANIES DISTRIBUTE DIVIDENDS AND SHAREHOLDERS DECIDE WHETHER TO REINVEST OR, AS IS NORMALLY THE CASE, INCREASE PURCHASES OF DURABLE GOODS.

4. SHIFT IN FUNDS FROM BANK TIME DEPOSITS, IF SUBSTANTIAL, MAY CAUSE PROBLEMS. ONE BANKER CLAIMED SYSTEM ALREADY RELATIVELY ILLIQUID. HE NOTED THAT RATE ON OVERNIGHT INTER-BANK MONEY, I.E., EQUIVALENT OF US FEDERAL FUNDS MARKET, ROSE FROM 0.6 PERCENT PER MONTH LAST WEEK TO 1.5 PERCENT EARLY THIS WEEK.

5. REASONS FOR GOVERNMENT ACTION DESCRIBED IN BOTH ECONOMIC AND POLITICAL TERMS. GOB CLEARLY WISHES TO REVIVE MARKET IN ORDER TO CAPITALIZE EFFECTIVELY ON SAVINGS AND TO COMPENSATE FOR EXPECTED DECLINE OF FOREIGN CAPITAL INFLOW. POLITICALLY, PRESENT ADMINISTRATION HAS BEEN SOMEWHAT EMBARRASSED BY ITS INABILITY TO REVIVE CAPITAL MARKET AND, THEREFORE, WOULD LIKE TO DO SO BEFORE LEAVING OFFICE.  
CRIMMINS

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